APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

No. 7422

ARTURO FORNARIS, JR., *Plaintiff, Appellee,*

v.

THE RIDGE TOOL CO. ET AL., *Defendants, Appellants,*

and

THE COMMONWEALTH OF PUERTO RICO, *Intervenor.*

Appeal from the United States District Court
for the District of Puerto Rico

Before ALDRICH, *Chief Judge,*
McENTEE and COFFIN, *Circuit Judges.*

March 17, 1970.

ALDRICH, *Chief Judge.* On June 24, 1964 the Puerto Rico legislature enacted the so-called Dealer's Contract Law known as Law 75. 1964 Laws of Puerto Rico, 4th Sess., at 231 (approved June 24, 1964). Its exact terms we will come to presently, but in effect this statute provided that a Puerto Rico dealer's contract with a "principal," hereinafter manufacturer, regardless of its provisions for termination was, with certain exceptions, renewable

indefinitely at the option of the dealer, and imposed substantial damages upon a manufacturer who refused to accede. On June 23, 1966 the scope of the obligation was enlarged to forbid the manufacturer from performing, irrespective of the provisions of the contract, "any act detrimental to the established relationship." 10 L.P.R.A. § 278a (1968 supp.). In spite of this legislation a number of manufacturers acted to terminate or otherwise change their dealers' agreements, and much litigation has ensued. Because of diversity of citizenship the bulk, apparently, of the cases were removed to the district court, where the defendants raised constitutional and other defenses. The court resolved these defenses in the plaintiff's favor in *Ruiz* v. *Economics Laboratory, Inc.*, D.P.R., 1967, 274 F. Supp. 14, and in the defendant's favor, in a more limited situation, in *United Medical Equipment Corp.* v. *S. Blickman, Inc.*, D.P.R., 1966, 260 F. Supp. 912. In the *Blickman* case the plaintiff appealed, and because of the great importance of the legislation we issued a general invitation for amicus briefs. Many were filed. We specially invited the Commonwealth to brief and argue the question of constitutionality, which it graciously did.

After argument, but before we had completed our opinion, the *Blickman* case (No. 6876) was settled, mooting the appeal. Thereafter we were asked to accept an interlocutory appeal in the present case pursuant to 28 U.S.C. § 1292(b). The parties did not request oral argument. By order we took the appeal on the briefs of the parties and transferred all earlier briefs, amicus and otherwise, filed in the *Blickman* case. We invited the Commonwealth to file a supplemental brief, which it has done. In addition, we have the benefit of the opinion of the Puerto Rico Superior Court in *Construction Mach. & Supplies Corp.* v. *Construction Mach. Co.*, decided December 23, 1968, upholding the act's constitutionality.

In the present complaint plaintiff Fornaris, a citizen of Puerto Rico, alleges that for twenty-nine years he had been

the exclusive distributor in Puerto Rico of merchandise manufactured by the defendant The Ridge Tool Company, an Ohio corporation; that on November 26, 1965, effective as of April 15, 1966, defendant "cancelled and/or terminated, without just cause the distributorship contract," contrary to the law of Puerto Rico.[1] It is not alleged that the termination was contrary to the terms of the contract itself, and we assume that it was in accordance therewith, and that plaintiff's rights depend solely upon Law 75. Defendant moved to dismiss on the ground that this law is unconstitutional, stating various reasons therefor. The court denied the motion on the basis of its opinion in *Ruiz* v. *Economics Laboratory, Inc.*, *supra*, and defendant appeals.

Before considering the precise terms of Law 75 it is pertinent to review the circumstances that led to its passage, and the declared purposes sought to be achieved. The legislature appended the following statement.

"STATEMENT OF MOTIVES

"The Commonwealth of Puerto Rico can not remain indifferent to the growing number of cases in which domestic and foreign enterprises, without just cause, eliminate their dealers, concessionaries [sic], or agents, as soon as these have created a favorable market and without taking into account their legitimate interests.

"The Legislative Assembly of Puerto Rico declares that the reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare, and in the exercise of its police power it deems

[1] This must have meant Law 75, as plaintiff's action was prior to the 1966 amendment. We do not, in this opinion, reach the amendment except to observe the obvious, that it presents many additional problems.

it necessary to regulate, insofar as pertinent, the field of said relationship, so as to avoid the abuse caused by certain practices."

We take this statement to be a summary of, and to represent an adoption of, the unanimous Report of the Committee on Industry and Commerce recommending the act in the form that it was eventually passed. The committee stated that it proposed the law because terminating dealerships "as soon as these have created a favorable market for their products, frustrat[ed] the legitimate expectations and interests of those who have so efficiently fulfilled their responsibilities."[2] See, generally, 18 Diario de Sesiones, Asambla Legislativa (Camara), May 22, 1964, pp. 1723-25. With respect to the "reasonable stability in the dealer's relationship," further amplification is to be found in 34 Rev. Jur. de la U.P.R. 497, quoted at length in the *Construction Machinery* opinion. Briefly, it was felt that cutting off dealers, with the manufacturer establishing its own sales office or branches, leads to instability of local investments and to the export of profits. Conversely, if manufacturers can terminate with impunity, some may withdraw altogether. Some Puerto Rico branches are marginal compared with other branches in the United States, and consequently are the first to be closed in case of declining business, to Puerto Rico's detriment.

We have gone into this background supplied by the parties not only because it shows the purposes of the act, illuminating the propriety, or possibly, impropriety, of its provisions, but also because of the assistance it may give in resolving doubts as to the statutory meaning. Law 75 itself is relatively brief. A manufacturer may never terminate, regardless of the provisions of the contract, or refuse to renew the dealership on an agreed expiration date, except for "just cause." Law 75, § 2, 1964 Laws of Puerto

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[2] For this, and certain other quotations, we rely upon translations from the Spanish furnished by various parties and not contradicted.

Rico at 232 (approved June 24, 1964).[3] "Just cause" is legislatively defined as substantial failure of performance by the dealer.[4] In case of breach of the statutorily imposed obligation, damages "shall be fixed on the basis"[5] of a specified list of items. Law 75, § 3. These are substantial, particularly with respect to awarding the dealer the entire good will value of the agency without inquiry or adjustment for what portion may have been due to the acts of the manufacturer, or even of prior dealers. To this figure is added, cumulatively the Commonwealth concedes, the amount of profits for the past five years. Law 75, § 3(d).[6] There is no provision for mitigation should it appear that the dealer had successfully transferred into an equally profitable line. Even apart from such lack of offsets, the award of both good will and loss of profits amounts to duplication. The parties are precluded from agreeing otherwise. Law 75 § 4.

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[3] "Notwithstanding the existence in a dealer's contract of a clause reserving to the parties the unilateral right to terminate the existing relationship, no principal or grantor may terminate said relationship or refuse to renew said contract on its normal expiration, except for just cause:"

[4] "[J]ust cause: nonperformance of any of the essential obligations of the dealer's contract, on the part of the dealer, or any action or omission on his part that adversely and substantially affects the interests of the principal or grantor in promoting the marketing or distribution of the merchandise or service." Law 75, § 1(d).

[5] It was conceded during the oral argument of the *Blickman* case that the Spanish, "se fijara a base" is mandatory.

[6] If the dealer has been in business less than five years, an appropriate multiple is provided to determine the equivalent of five years. It may be noted that the effect of this provision is exactly to contradict the declared reason for the act—that dealers are cut off "as soon as they have developed a favorable market." On that basis their past profits would be negligible. If, however, the dealer had not received this unfortunate treatment, but had been permitted a long, prosperous career to reward him for his entrepreneur services, then his award under this section would be substantial.

In upholding the constitutionality of the application of the act to the present defendant the district court, as did the superior court in the comparable case, relied upon the police power. There can be no question but that this power permits the legislature to remedy various economic evils. All courts recognize, however, that retrospective legislation, affecting established rights and relationships, presents an additional problem. While the legislature may prevent an employee willing to contract to work for a low wage from doing so, *West Coast Hotel Co.* v. *Parrish*, 1937, 300 U.S. 379, the retrospective imposition of a minimum wage would be quite a different matter. *See Luce & Co.* v. *Minimum Wage Board*, 1943, 62 P.R.R. 431, *aff'd* 1 Cir., 1946, 155 F.2d 983, where the court stated, in dictum, that a statute granting additional benefits for "services entered into and executed . . . before the same went into effect . . . would be unconstitutional, since it would deprive the employers of their property without due process of law." 62 P.R.R. at 449. We cannot agree with the many arguments, variously advanced, that the case at bar does not involve similar retrospectivity. If at the time that Law 75 was passed a manufacturer had contracts with dealers that he could terminate at will without liability, and thereafter, because in the opinion of the legislature such a result would deprive the dealers of their expectations based upon their having "so efficiently fulfilled their responsibilities" it must make substantial payments on termination, we can only regard this as increased payment for past services. Indeed, if it is not, it is an amendment of the contract to require an outright gratuity.

We need not deal with a constitutional prohibition against impairing the obligation of contracts,[7] because the due

[7] The argument goes that Puerto Rico is not subject to certain constitutional restrictions because not a "state." *Cf. Buscaglia* v. *Ballester*, 1 Cir., 1947, 162 F.2d 805. However, the Puerto Rico Constitution contains a provision comparable in this respect to the federal Bill of Rights. Puerto Rico Constitution Art. II, § 7. Since

process clause of the federal constitution provides essentially the same restraint so far as retrospectivity is concerned.[8] We have no thought that Puerto Rico is in a more favored position in this respect than is a state or the federal government. *Figueroa Ruiz* v. *Delgado*, 1 Cir., 1966, 359 F.2d 718, 723-24, *Mora* v. *Mejias*, 1 Cir., 1953, 206 F.2d 377, 382. *See* 48 U.S.C. § 731d; Joint Resolution, 66 Stat. 327. (July 3, 1952). Hence only minor infringement of established contractual rights may be effected without just compensation. "Police power" is not a magic word that permits the legislature to adjust any and every found economic ill without payment.

In determining whether retroactive alteration of contractual provisions are sufficiently minor to be permissible a distinction is sometimes drawn between alteration of substantive rights and alteration of procedures or remedies. *See Stockholders of Peoples Banking Co.* v. *Sterling*, 1937, 300 U.S. 175, 180-83 (alternative holding). However, even the latter may infringe constitutional rights, Hale, *supra* n. 8, at 533-57, *W. B. Worthen Co.* v. *Kavanaugh*, 1935, 295

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this provision might be said to have been imposed by Congress, see Act Mar. 2, 1917, c. 145, § 2, 39 Stat. 951, as amended, 41 Stat. 1096, 47 Stat. 158, 48 Stat. 361, 61 Stat. 772, repealed, except for last paragraph, Act July 3, 1950, c. 446 § 5(1), 64 Stat. 320, an argument might be made in favor of the federal court's interpretative and enforcement powers by one route or another. By suggesting the question we do not suggest the answer.

[8] "Although there is no clause expressly forbidding the federal government to pass laws impairing the obligation of contracts, any federal law impairing them in a manner which the Supreme Court deemed unreasonable would doubtless be held to be a deprivation of property without due process, contrary to the Fifth Amendment." Hale, The Supreme Court and the Contract Clause: III, 57 Harv. L. Rev. 852, 890 (1944). *Accord*, Hochman, The Supreme Court and the Constitutionality of *Retroactive Legislation*, 73 Harv. L. Rev. 692, 695 (1960). *Cf. Lynch* v. *United States*, 1934, 292 U.S. 571, 579; *Thorpe* v. *Housing Authority*, 1969, 393 U.S. 268, 278-79, nn. 31-32.

U.S. 56, while the former can sometimes be tolerated if the effect is not too severe. *El Paso* v. *Simmons*, 1965, 379 U.S. 497, 503-08. Essentially, the question is, how drastically have property rights been affected, and, particularly, how great is the change viewed in the light of the reasonable expectations of the parties when the contract was entered into. *See El Paso* v. *Simmons, supra; Home Bldg. & Loan Ass'n* v. *Blaisdell*, 1934, 290 U.S. 398. The distinction is one of degree. For example, emergency statutes allowing a tenant to stay beyond the term of his lease upon payment of reasonable rent have been upheld as reasonable alterations, *Block* v. *Hirsh*, 1921, 256 U.S. 135; *Marcus Brown Holding Co.* v. *Feldman*, 1921, 256 U.S. 170, whereas a statute which would have destroyed a mining company's reserved right to mine coal underneath land, the balance of which had been sold by it, has been invalidated as working a change of too great magnitude. *Pennsylvania Coal Co.* v. *Mahon*, 1922, 260 U.S. 393. See generally *Hochman, supra* n. 8, at 711-17.

While we recognize a strong obligation to support legislative findings, the Report of the Committee on Industry and Commerce to the effect that the termination of dealerships in terms revocable at will was "frustrating the legitimate expectations" of the dealers cannot possibly be true. Dealers may have had hopes; they could have no legitimate expectation of non-terminable contracts. *Cf. Castillo* v. *Smart Products, Inc.*, D.P.R., 1968, 289 F.Supp. 138. Sounding phrases, and calling the failure to make termination payments an "abuse," cannot change the fact that the manufacturer has been forced into heavy contractual obligations that it never assumed. No amount of research by parties or amici has discovered a case suggesting that to convert a contractual relationship terminable by either party without cause into one which, short of breach by the other party, can be terminated by one of the parties only by making substantial payments and without protection

for the other party's economic interests, is not a change of great magnitude.[9]

We do not agree with the position of the opponents of the act that the phrase "just cause" is unconstitutionally vague and unspecific. However, the Commonwealth's protestation, in the *Blickman* brief, that it "cannot conceive that the Legislature, which was enacting a remedial statute to correct an injustice, could have intended and permitted, through legislation, the perpetration of another injustice," is far more pious than persuasive. To our comment that the statute is one-sided, the Secretary of Justice on behalf of the Commonwealth, urged us to read it in the light of various general provisions of Puerto Rico law applicable to the construction of contracts. This we have done. We end up convinced that the only defense open to a manufacturer to an action under Law 75, short of proof of breach by the dealer, would be impossibility of performance. 31 L.P.R.A. § 3193. To add to "just cause," as was suggested, good faith, or the legitimate interests of the manufacturer, would be to fly in the face both of the unambiguous statutory provisions, and the equally unambiguous legislative history. The fact that a dealership has become economically highly disadvantageous is not excusable impossibility, but is, precisely, a contingency that the legislature sought to guard against.

Some of the proponents of the act invite a comparison with the federal Automobile Dealers Day in Court Act, 15 U.S.C. § 1221-25, hereinafter the Federal Act. The comparison is ill-taken. In fact, it is precisely to the extent

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[9] If we may be forgiven a rude comparison, the change seems comparable to a legislative retrospective conversion, in the asserted interest of public morals, of all temporary liaisons into marriage, with the necessity of divorce and alimony. Indeed, it is worse, for until Law 75 was enacted temporary dealerships were in all respects legal.

that Law 75 departs from the provisions of that statute that it is in difficulties.

The unusual position in which automobile dealers find themselves has long been known to this court.[10] Because they are normally locked in, with no other source of income and no easy opportunity to convert to other lines, an unscrupulous manufacturer is able to take advantage of its dealers by making unjustifiable demands, such as requiring needlessly large showrooms, or the purchase of undesired parts or models, under threat of cancellation of the dealership. It was found that many manufacturers were engaging in such practices. See generally, Kessler, Automobile Dealer Franchises: Vertical Integration by Contract, 66 Yale L.J. 1135 (1957). The Federal Act did not seek to convert terminable automobile dealers contracts into non-terminable ones, but was tailored to prevent contractually unjustified demands by giving a cause of action for damages resulting from unfair "coercion" and "intimidation." 15 U.S.C. § 1221(e). Absent such improper behavior, any action within the terms of the contract remained permissible, including outright termination without proof of grounds therefor. *Berry Bros. Buick, Inc.* v. *General Motors Corp.*, E.D.Pa., 1966, 257 F.Supp. 542, 546, *aff'd mem.* 3 Cir., 1967, 377 F.2d 552; *cf. Southern Rambler Sales Inc.* v. *American Motors Corp.*, 5 Cir., 1967, 375 F.2d 932, *cert. denied* 389 U.S. 832; 15 U.S.C. §§ 1221, 1222.

By contrast, Law 75 applies to every kind of dealer across the board. As pointed out in the memorandum opinion of the district court in *Felix A. Rodriguez, Inc.* v. *Bristol-Myers Co.*, D.P.R. 2/13/68, many types of dealers carry numerous articles and lines, or can readily convert and absorb the loss of a single manufacturer. Such dealers are not subject to pressure by threats of cancellation. Nor

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[10] *See Volkswagen Interamericana, S.A.* v. *Rohlsen*, 1 Cir., 1966, 360 F.2d 437, *cert. denied* 385 U.S. 919; *Young Motor Co.* v. *Com'r*, 1 Cir., 1960, 281 F.2d 488.

was the Puerto Rico act framed in terms of illegitimate demands—except to say that adherence to the contract terms was itself illegitimate. By labelling the exercise of express contractual rights "unjust" the legislature was not giving a cause of action for contractual abuse; it was rewriting the contract.

Comparing Law 75 with the Federal Act in terms of retrospectivity is, in a sense, merely an intellectual exercise. The parties have cited no case holding even the Federal Act constitutionally retrospective. Non constat, in the light of the differences, that it might properly be so held had the question arisen.[11] Law 75, however, cannot be.

The judgment of the District Court is vacated. Judgment for the defendant.

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[11] We do not reach the question of non-retrospective application of Law 75, as we may wonder how many such dealerships have been established. Since the provisions of the law are non-waivable, manufacturers who are unwilling to accept them will not enter into dealership contracts at all, and dealers who would prefer to have dealerships omitting such benefits rather than have none, have lost, to that extent, their freedom of contract. It is possible that if the legislature had realized that the law could be applied only prospectively it would not have enacted it. With this matter, however, we are not presently concerned.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

Civil No. 546-66

Re: DAMAGES

ARTURO FORNARIS, JR., *Plaintiff*

v.

THE RIDGE TOOL COMPANY and
THE RIDGE TOOL INTERNATIONAL COMPANY, INC.,
Defendants

THE COMMONWEALTH OF PUERTO RICO, *Intervenor*

Memorandum and Order

On March 12, 1968 this Court entered an order staying proceedings in this action pending determination of an action entitled *United Medical Equipment Corporation v. S. Blickman, Inc.*, which at that time was pending before the Court of Appeals for the First Circuit, Case Number 6876, and wherein the constitutionality of Law Number 75 of June 24, 1964, as amended (10 L.P.R.A. 278), was being challenged on the same grounds as those raised by the defendants in this case through their motion to dismiss. The matter of the constitutionality of the Dealer's Act was fully briefed and oral argument was had before the Court of Appeals, but the case was settled prior to decision.

A similar fate befell the case of *Carmac Chemical Corporation v. Application Engineering Corporation* (Court of Appeals for the First Circuit, Case Number 7177). In this case, the First Circuit, as per Order of Court, August 29, 1968, took the position that it would appreciate an opportunity to consider the views of at least the Superior Court of Puerto Rico on the constitutionality of the Dealer's Act. Accordingly, it neither allowed nor denied

the interlocutory appeal and stated that upon receipt of any decision and opinion from the Superior Court of Puerto Rico, and upon a joint stipulation or a deposition or other showing of the terms, conditions and surrounding circumstances, the Court would again consider the application for leave to appeal in the *Carmac* case. Once again the parties settled the case and there is now no case pending before the United States Court of Appeals which raises the constitutionality of the Dealer's Act.

The matter of the constitutionality of the Dealer's Act has now been passed upon by the Superior Court of the Commonwealth of Puerto Rico in the case of *Construction Machinery and Supplies Corporation* v. *Construction Machinery Co.*; Civil Number 67-3549. A translation of this case is set out as Exhibit A to this order, and made to form a part hereof by reference.

A motion for reconsideration of the Superior Court Order was denied on March 11, 1969 by said Tribunal.

In view of the foregoing developments, this Court ordered that this case be set for some disposition and set a hearing thereon for June 13, 1969. By motion dated June 9, 1969, attorneys for the plaintiff requested that on the basis of the decision rendered by the Superior Court of Puerto Rico in the case of *Construction Machinery and Supplies Corp.* v. *Construction Machinery Co., supra,* and on the basis of this Court's prior decision upholding the constitutionality of the Dealer's Act of Puerto Rico we order the dismissal of defendant's motion to dismiss and order the defendants to file their answer to the complaint filed in this case.

We agree with plaintiff that the motion to dismiss should be denied on the basis of our prior decision in this area [*Ruiz* v. *Economics Laboratory, Inc.*, 274 F. Supp. 14 (1967)]. This Court is of the opinion that the order of dismissal of the constitutional defense raised by the defendants involves a controlling question of law as to which there is substantial ground for difference of opinion

in this jurisdiction and that an immediate appeal from this order may materially advance the ultimate termination of this litigation and of many others presently pending in this Tribunal. In conformity with 28 U.S.C.A. § 1292(b) and inasmuch as a rapid adjudication of the constitutionality of the Dealer's Act is not only in the best interests of the parties to this action, but is also in the furtherance of justice, it is hereby

ORDERED

1. Defendant's motion to dismiss on constitutional grounds is denied (*Ruiz v. Economics Laboratory, Inc.*, 274 F. Supp. 14 (1967); *Construction Machinery and Supplies Corp. v. Construction Machinery Co.*, Civil Number 67-3349, Superior Court of Puerto Rico, San Juan Part).

2. This Court is of the opinion that this order involves a controlling question of law as to which there is substantial grounds for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation. Accordingly, this Court hereby so states as required by Section 1292(b) of Title 28 U.S.C.A.

3. All further proceedings in this case are stayed until further order of this Court.

San Juan, Puerto Rico, this 8th day of August, 1969.

HIRAM R. CANCIO
Hiram R. Cancio
Chief Judge
United States District Court

IN THE SUPERIOR COURT OF PUERTO RICO
SAN JUAN PART

Civil No. 67-3549

Re: DAMAGES

CONSTRUCTION MACHINERY & SUPPLIES CORPORATION,
Plaintiff

v.

CONSTRUCTION MACHINERY CO.,
Defendant

COMMONWEALTH OF PUERTO RICO,
Intervenor

Opinion

The matter before the court is a special defense filed by defendant in this case on May 13, 1968 in which there is alleged the unconstitutionality of Law #75 of 1964, as amended.[1]

[1] The circumstances that led to the intervention by the Legislature of Puerto Rico are amply set forth in 34 Rev. Jur. de la U. P. R. p. 497. The following appears there:

"Law No. 75 of June 24, 1964 is of great importance for contractual relationships between principals and distributors in Puerto Rico. We shall study two aspects of it. First, the manner in which said contracts are affected by the law. Second, the constitutional issues raised by the same. This second part of the study will be carried out by means of a comparative analysis of other similar laws that are in effect in different jurisdictions of the United States. Similarly, the jurisprudence which has arisen in connection with these statutes will form a part of our analysis.

The social ill that this piece of legislation seeks to correct is based upon the fact that a great number of distributors based in Puerto Rico have been eliminated as factory representatives. This tendency caused the voices of the Chamber of Commerce of Puerto Rico and of the individual distributors to be heard in protest against the existing situation. Said

After having studied the memoranda of the parties, as well as the oral argument, we may pass on to consider the allegations.

I. The defendant alleges that Act No. 75 of 1964 impairs the obligations of contracts existing at the time of its approval.

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tendency is characterized by two types of situations: principals or grantors that arbitrarily cancel the distribution contracts of businessmen established in Puerto Rico; and the factories that decide to open their own sales offices or branches. The distributors faced these problems espousing several arguments. This group maintains that the development of a market for the represented products requires great sums of money. That once the products are on the market, the factories, not withstanding the effort and the capital invested, cancel the contracts and establish themselves here without providing any indemnity whatever. It is pointed out that the system by means of which the manufacturers establish sales offices or branches creates an instability that impedes the strengthening of the field of local capital investment. It is also said that when branches or sales offices are established, these export a large part of the profits earned in Puerto Rico.

Some of the established branches are classified as marginal branches. These are the sales offices located in markets that are small when compared to other branches in the United States. They are the first to be closed in time of emergency, which would force Puerto Rico to recur directly to the north-american market to obtain indispensable items, especially in the field of industry. This class also incurs greater general expenses relative to sales and the product which would result in a price increase and a reduction in services.

Local distribution serves as an incentive to those persons who want have their own business. A manager of a branch cannot become interested in the problems, ambitions and needs of our community. The distributors claim that the manager of a branch has as his purpose the securing of a promotion to be sent to another country or to the home office as an executive and, for that reason, is not interested in the well-being of the Puerto Rico economy. The persons in charge of the sales office do not fully know the motivations or factors that motivate the decisions that must be put into effect, inasmuch

In support of this allegation the defendant cites the provisions of Article 1207 of the Civil Code and the first article, tenth section of the Constitution of the United States of America and the second article, seventh section of the Constitution of the Commonwealth of Puerto Rico.

The provisions cited above have not been violated by this Law of the Legislature of Puerto Rico. It is a principle

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as these are made by the Board of Directors at the home company. Said decisions may very well result in a detriment to the Puerto Rico market due to the fact that standards and methods used in the northamerican nation are not necessarily applicable to our market. The distributor established in Puerto Rico by his very nature and experience is more familiar with the country's market. We can say that he knows the psychology of the consumer. As a result this singular position allows the person to adequately determine the preferences of the consumer in terms of the type of product desired and the amounts that may be consumed, thus maintaining a beneficial balance for the economic stability of our community.

'Those who are opposed to a system of distribution of products and services through exclusive distributors claim that it 'is an unnecessary and expensive middle step that only contributes to an increase in the costs of distribution.' The opposing side argues that it is 'an indispensable factor for the marketing system. This is based upon the following: 'Due to our insular condition to the fact that our market is separated from the principle sources of supply by an enormous stretch of sea, to our geographical smallness and lack of natural resources and because potential sales and business volume in our island is relatively small, to the manufacturer it would normally be uneconomic to eliminate the exclusive agent or distributor and establish its own branch for sales, or to sell to consumers from its point of origin or to local wholesalers and retailers. The exclusive agent or distributor is a functional intermediary that with the exception of certain isolated cases, may not be eliminated or cut back without causing injury to the efficiency and costs of our distribution system, for they render important services in an atmosphere of competition to the producer and the consumer in a manner more efficient and economic than the very manufacturers.'

The circumstances set forth above led the legislature to act. It was forced to resolve the problem put to it by a pressure

recognized by the courts of Puerto Rico and of the United States of America that this right of freedom of contract is not one without limit of any kind. The same is conditioned by the police power of the state. Article 1207 of our Civil Code contemplates this when it provides that:

> "The contracting parties may make the agreements and establish the clauses and conditions which they may deem advisable, provided they are not in contravention of law, morals or public order". (31 LPRA 3372)

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group: the need to stop the principals, or at least to seek indemnification for the distributors. It was the practice to include a clause in which it was provided that either of the parties by means of 30, 60, or 90 days notice could cancel the existing relationship. The principal, making use of its bargaining power, managed to include in the contract this and other clauses favorable to it.

In order to remedy this situation, the Legislative Assembly of Puerto Rico, invoking the police power of the State, approved the law now before us for the purpose of regulating the termination of distribution contracts and a refusal to renew the same. The statute expressly provides that no principal or grantor may unilaterally terminate a distribution contract or refuse to renew the same without just cause, notwithstanding any agreement to the contrary.

If the principal or grantor terminates the contractual relationship, without just cause, it must indemnify the distributor. The rights granted by the law are of a public nature, and therefore not waivable. All actions based upon the law prescribe in three years reckoned from the date of the definitive termination."

In light of the foregoing examination it is evident that the problems and needs of Puerto Rico are in large measure different from those of the United States of America and the existing relationship between the two requires a more equitable and special consideration in order to arrive at the conclusions of this opinion. We can not forget that Puerto Rico is a small island (3,500 square miles), tropical, with few natural resources, depending, for this reason, greatly upon business".

In *Manigault* v. *Spring*, 199 U.S. 473 (1905), it was noted that:

> "This power . . . is an exercise of the sovereign right of the government to protect the lives, health, morals, comfort, and general welfare of the people, and is paramount to any rights under contracts between individuals".

Reference may also be made to *Sierra* v. *San Miguel*, 1949, 70 P.R.R. 573, in which the Honorable Supreme Court of Puerto Rico referring to the same question notes that "no rule is more firmly embedded in our constitutional law than this doctrine". See further, *Veil* v. *Sixth Ward Building*, 310 U.S. 32; *Anderson* v. *Brand*, 303 U.S. 95; *City of El Paso* v. *Simmons*, 379 U.S. 497.

Law No. 75 was created to remedy an existing "grave situation" that would still exist if it were not for the promulgation of said law. See page 1531 of the Record of Meetings of the Legislative Assembly of Puerto Rico of 1964 where it is said:

> "Your Committee on Industry and Commerce has considered the substitute to S. B. 673 and has the honor of proposing that it be approved without amendment.
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> The problem created in the system of distribution in Puerto Rico by the intemperate action of foreign and domestic business concerns that, without just cause, cancel their relationships with their distributors and agents in Puerto Rico, as soon as those have created a favorable market for their products, frustrating the legitimate expectations and interests of those who have so efficiently met their responsibilities, has recently worsened.
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> Normally, the agency or distribution contract is drafted by the manufacturer with clauses favorable to it, and a provision to the effect that the relationship may be terminated by either of the parties, by means

of prior notice of sixty or ninety days. The distributor or agent efficiently devotes himself to opening the market for the represented product, and, when he begins to derive benefits from the operation, once the market is established, the manufacturer realizes that it would be economically favorable to establish its own sales office or its own branch, and in an unjust manner, without equitable compensation for the efforts expended by the distributor or agent, cancels the relationship. In other cases, the manufacturer finds another person who, the business being established, is willing to distribute the product for less compensation, because he doesn't have to make the initial investment, and is not subject to the risks of the prior distributor or agent.

The traditional provisions which regulate contracts between private parties have shown themselves to be incapable of protecting the legitimate rights of the distributor or agent, and for this reason it has become necessary to legislate to regulate this relationship and guarantee that the manufacturers will act in good faith, equitably, in a non-arbitrary manner, and to preserve for the distributor or agent the legitimate rights and expectations inherent in the relationship. Moreover, this will result in greater stability for the distribution relationship.

This is the grave situation that is sought to be remedied by the approval of this bill. The Department of Commerce of the Commonwealth of Puerto Rico, the Chamber of Commerce of San Juan, and the Agency for Industrial Development regard with accord and heartily endorse the protection and stability that would be given to the relationships between manufacturers and their distributors if this bill should be approved.

The Committee, unanimously, agreed to recommend the passage of this bill".

The defendant has noted that in said legislation the word "emergency" has not been used to justify the existence of said legislation. The expression "grave situation" within our language and culture and the interpretation which this Court makes of the legislative intent has a meaning similar to the English term "emergency", assuming, but without deciding, that the appearance of this term is an indispensable requirement. The Spanish term "emergencia" as a translation of the English term "emergency" is an anglicism.[2]

In the case of *Willy's Motor v. Northwestern Kaiser-Willy's, Inc.*, 142 F. Supp. 469 (D.C.-1956), there was contested the constitutionality of a Minnesota statute which contained greater requirements as to the relationship between manufacturers and distributors and at the same time covered a more restricted area than that covered by Law No. 75. The Court, in sustaining the constitutionality of the Minnesota statute, noted that legislation enacted with a public purpose was not subject to attack under the Contracts Clause.

Law No. 75 has a public purpose, as can be clearly seen from its legislative history as well as from its statement of motives;[3] for this reason, we are of the opinion that the

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[2] The Dictionary of the Royal Academy, eighteenth edition, defines the term "'emergencia' as the act or result of emerging, occurrence, a supervening accident.

[3] "Statement of Motives"

The Commonwealth of Puerto Rico can not remain indifferent to the growing number of cases in which domestic and foreign enterprises, without just cause, eliminate their dealers, concessionaries, or agents, as soon as these have created a favorable market and without taking into account their legitimate interests.

The Legislative Assembly of Puerto Rico declares that the reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare, and in the exercise of its police power, it deems it necessary to regulate, in as far as pertinent, the field of said relationship, so as to avoid the abuse caused by certain practices".

law does not suffer from the constitutional vice alleged and discussed above.

II. The defendant alleges as the second ground for the unconstitutionality of Law No. 75 that the Law violates the Due Process Clause as to manufacturers and that it is vague and imprecise as to its scope and definition of the term "just cause".

The standard to be used must be the reasonableness of the legislation. If the measure which we are considering is justified by social, economic, health, or general welfare considerations, and it is reasonable—the statute must be considered to be invulnerable to attacks of this sort.

In the case of *Blanke Brothers* v. *Ford Motor Co.*, 203 F. Supp. 670 (1962), the Court concluded that "the fact that Congress . . . gave the dealer a remedy . . . without giving the same remedy to the manufacturer, is not violative of the due process clause . . . .". See to the same effect the case of *Kuhl Motors Co.* v. *Ford Motor Co.*, 71 N.W. 2d 420.

III. The defendant alleges that Law No. 75 in its definition of just cause is unreasonable, arbitrary and capricious vague and imprecise. Said definition is not limited to its literal content. It constitutes a guide to the Court so that it may decide in the light of the facts of each particular case whether or not there existed just cause. This concept of just cause just like the concept of the reasonable man and the good head of a family is not a new concept in our law.

In the cases of *P. R. Cap. S. Tire Sales* v. *District Court*, 1948, 68 P.R.R. 370; *Avilés* v. *District Court*, 1948, 69 P.R.R. 106; *Blanes* v. *District Court*, 1948, 69 P.R.R. 106; *Mercedes Bus Line, Inc.* v. *District Court*, 1949, 70 P.R.R. 656, our Supreme Court considered the concept of "just cause" in accordance with the facts of each case brought

before its consideration. In each of these cases it can be appreciated how wide this concept of just cause is, as well as its usefulness in our system. The use of this concept in various laws is due to the fact that the legislature cannot foresee every possible fact situation when it drafts a law, leaving this function to the courts who must decide in accordance with the particular facts of each case. This Court cannot understand that the legislator has imposed as the only reason justifying a cancellation of the relationships the reasons which make up the definition of just cause.

This concept of just cause, in its turn, should further be supplemented, when a case may merit it, with statutory precepts drawn from other laws of the State. Such would be the case of a manufacturer who for economic reasons cannot continue to sell its products in our market. In a situation like this one, this Court is of the opinion that it would be necessary to go beyond the law and make applicable the provisions that are relative to the impossibility of performance contemplated by our Civil Code, in Art. 1138 (31 LPRA 3193). See *Rodríguez* v. *Municipality*, 75 P.R.R. 449; where the Supreme Court of Puerto Rico says that:

> "The impossible performance is produced when, having examined the circumstances on which a contract is signed and the circumstances on which it should be subsequently performed, it appears that its subsequent performance is not possible because of the supervening circumstances which did not exist at the time of contracting the obligation".

Summarizing, this concept of just cause must be interpreted case by case and always depending upon the particular facts of each one.[4] Obviously our own juridical

[4] Recently the Federal District Court for Puerto Rico, by the Hon. Judge Fernández Badillo expressed the same thought in the case of Schering Transamerican Corporation vs. Wallace Torres

system provides for cases in which compliance becomes impossible, and for this reason it is not correct to suppose that Law No. 75 of 1964 is unjust or oppressive in its terms.

There is nothing in the law that might be interpreted as indicating that the Legislature of Puerto Rico is discriminating against firms operating in interstate commerce. The law applies both to local firms and continental ones doing business in Puerto Rico. The present legislation is clearly within the police power which the Commonwealth of Puerto Rico possesses and within the clear intention of the Legislature of Puerto Rico to protect its citizens and businessmen.

It is worthy of note that in our commercial relations with the United States, Puerto Rico has received special treatment from the United States. Examples of this, among others, are the tariff laws dealing with sugar, coffee and rum exported from Puerto Rico. These and other similar laws, are founded upon the geographic and economic conditions of Puerto Rico and the lack of adequate natural resources, all of which has justified the special treatment as regards the other states of the Union.

IV. Defendant alleges that Law No. 75 violates the equal protection clause. The defendant further argues in its brief that the law in question operates for the sole and exclusive benefit of those distributors in existence at the

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Canet vs. Sutton Cosmetics, et. al., Civil No. 542-66 in noting in its opinion of September 30, 1968 the following:

"Defendant does not claim that Sutton Cosmetics could not have whatever arrangement it had with him. Certainly when Sutton Cosmetics went out of business, that was ample 'just cause' to terminate whatever relationship they had'.

"Nor does it preclude a state from giving needful protection to its citizens in the Course of their contacts with business conducted by outsiders when the legislation by which this is accomplished is general in its scope, is not aimed at interstate or foreign commerce, and involves merely burdens incident to effective administration'.

time of its approval and that the manufacturers may not appoint additional distributors.

The equal protection clause does not imply that at any given moment the Legislature of a country may not establish a counterbalance in favor of a disadvantaged class.

In the case of *Kuhl Motor Co.* v. *Ford Motor Co.* (supra), the following was noted:

> "The fact that the persons to be benefited by this regulatory measure are confined to one class of our citizens, auto dealers, does not militate against the same being a legitimate exercise of the police power".

There exists in Puerto Rico and the United States a great quantity of legislation which is directed to the benefit of a particular class of individuals or persons. To contend that this may not be done is to bind the arms of the State in its mission to make all citizens equal in law.

There is nothing in this law that would lead this Court to think that new distributors may not be appointed inasmuch as the statute does not prohibit such action. What the law regulates is the termination of the existing relationship; or directly or indirectly executing an act which impairs the established relationship; or a refusal to renew said contract upon its normal expiration. (10 L.P.R.A. 278a).

The case before us does not involve the appointment of an additional distributor. It deals with the termination of a distribution contract. At the proper moment we will decide whether there existed or not just cause. There may be circumstances in which the appointment of a new distributor constitutes an impairment of the established relationship, but courts should not deal with hypothetical situations. This Court is of the opinion that if the manufacturer or principal names a new distributor and there is no impairment of the existing relationships between it and

the original distributor, said distributor is totally lacking a cause of action under this law. We have already said that Law No. 75 is one which should be interpreted case by case and that only after the presentation of the whole evidence will the Court be in a position to determine whether there was an impairment of the existing relationship, or if there was a unjustified refusal to renew a contract or if a contract was terminated without just cause.

The defendant alleges that Law No. 75 creates a monopoly in favor of the distributor. We do not see the logic of this observation. When an act, or series of acts in a particular case result in a monopoly or monopolistic practices prohibited by law, we will decide that problem in the light of the particular case. Neither the legislative history of Law No. 75, nor Law No. 77 of June 25, 1964, known as the monopoly law, provide a basis for this assertion. These laws were enacted contemporaneously so the legislators were aware of the contents and language of each when they were approved.

In connection with the damages contemplated by Section 278.b of the law (Title 10 L.P.R.A.), we are of the opinion that the same does not limit the power of the Court to indemnify a distributor upon the basis of the factors set forth in the said section.

For the reasons set forth, the Court concludes that Law No. 75 of 1964, as subsequently amended meets the constitutional requirements. The special defense pleaded by the defendant is therefore denied.

Let service be made.

Given at San Juan, Puerto Rico, this 23rd day of December, 1968.

/s/ HÉCTOR RUIZ SOMOHANO
Superior Court Judge

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

CIVIL No. 7422

ARTURO FORNARIS, JR., *Plaintiff, Appellee*

v.

THE RIDGE TOOL COMPANY, ET AL., *Defendants, Appellants*

and

THE COMMONWEALTH OF PUERTO RICO, *Intervenor, Appellee*

Notice of Appeal to the Supreme Court of the United States

To the Honorable Court:

1. Notice is hereby given that the Commonwealth of Puerto Rico, Intervenor, Appellee above named, hereby appeals to the Supreme Court of the United States from the Judgment opinion entered by this Honorable Court on March 17, 1970.

2. This appeal is taken pursuant to 28 U.S.C. Section 1254(2). In San Juan, Puerto Rico, this 26th day of May, 1970.

APPENDIX D

[No. 75]

AN ACT

To regulate the termination of, and the refusal to renew, under certain circumstances, certain dealer's contracts.

STATEMENT OF MOTIVES

The Commonwealth of Puerto Rico can not remain indifferent to the growing number of cases in which domestic and foreign enterprises, without just cause, eliminate their dealers, concessionaries, or agents, as soon as these have created a favorable market and without taking into account their legitimate interests.

The Legislative Assembly of Puerto Rico declares that the reasonable stability in the dealer's relationship in Puerto Rico is vital to the general economy of the country, to the public interest and to the general welfare, and in the exercise of its police power, it deems it necessary to regulate, insofar as pertinent, the field of said relationship, so as to avoid the abuse caused by certain practices.

Be it enacted by the Legislature of Puerto Rico:

Section 1.—Definitions

For the purposes of this act, the following terms shall have the meanings expressed below, save when the context clearly indicates otherwise:

(a) dealer: person to whom is granted the distribution, agency, concession or representation of a merchandise or service for him to develop a market therefor and/or seek its sale or distribution in Puerto Rico;

(b) dealer's contract: relationship established between a dealer and a principal or grantor whereby the former takes charge of the distribution of a merchandise, or of

the rendering of a service, by concession or franchise, on the market of Puerto Rico;

(c) principal or grantor: person who executes a dealer's contract with a dealer;

(d) just cause: nonperformance of any of the essential obligations of the dealer's contract, on the part of the dealer, or any action or omission on his part that adversely and substantially affects the interests of the principal or grantor in promoting the marketing or distribution of the merchandise or service.

Section 2.—Notwithstanding the existence in a dealer's contract of a clause reserving to the parties the unilateral right to terminate the existing relationship, no principal or grantor may terminate said relationship or refuse to renew said contract on its normal expiration, except for just cause.

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Section 3.—If no just cause exists for the termination of the dealer's contract or for the refusal to renew same, the principal will have committed a tortious act against the dealer and shall indemnify him to the extent of the damages caused him, the amount of such indemnity to be fixed on the basis of the following factors:

(a) the actual value of the amount expended by the dealer in the acquisition and fitting of premises, equipment, installations, furniture and utensils, to the extent that these are not easily and reasonably useful to any other activity in which the dealer is normally engaged;

(b) the cost of the goods, parts, pieces, accessories and utensils in stock, and from whose sale or exploitation he is unable to benefit;

(c) that part of the good will of the business of the dealer attributable to the sale of the merchandise or

service the object of the dealer's contract to be determined by taking into consideration the following factors:

(1) the number of years the dealer has had charge of the distribution;

(2) the actual volume of the sale of the merchandise or service and the proportion it represents in the dealer's business;

(3) proportion of the Puerto Rican market said volume represents;

(4) any other factor that may establish equitably the amount of said good will;

(d) the amount of the profit obtained by the dealer in the sale of the merchandise or service during the last five years or, if less than five, five times the annual average of the amount of the profit obtained during the last years, whatever they be.

* * * * * * * * * * *

Section 4.—The provisions of this act are of a public order and therefore the rights determined by such provisions can not be waived.

Section 5.—Every action arising from this act shall prescribe in three years reckoning from the date of the definitive termination of the dealer's contract.

Section 6.—If any clause, paragraph, article, section or part of this act is declared unconstitutional by a court of competent jurisdiction, said judgment shall not affect, impair or invalidate the rest of this act.

Section 7.—This act shall take effect immediately after its approval.

Approved June 14, 1964, as amended June 28, 1965.